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# Commercial Property Finance



## Property Insights

### **FNB Commercial Property Broker Survey – 4<sup>th</sup> Quarter Survey points to a partial “post-COVID-19 hard lockdown” property recovery that is slow and unconvincing**

#### Key Points

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- The 4<sup>th</sup> Quarter of 2020 FNB Commercial Property Broker Survey saw all 3 major commercial property sectors, i.e. Industrial and Retail, showing slight increases in perceived market activity levels, with the Office Property Market’s Activity Rating still the weakest, and Industrial remaining the strongest.
- The percentage of respondents perceiving business conditions to be satisfactory declined in the 4<sup>th</sup> quarter survey to a very weak 21%, down from 31% in the previous quarter, following a mild 3<sup>rd</sup> quarter increase as the country emerged from the 2<sup>nd</sup> quarter hard lockdown.
- When asking brokers for their ratings of market activity levels on a scale of 1 to 10, we still see that the group of respondents is most upbeat (or least pessimistic) about the Industrial and Warehouse Property Market. The Industrial Property Market’s 4<sup>th</sup> quarter activity rating rose slightly, from 4.64 in the prior quarter to 4.68 in the 4<sup>th</sup> quarter. The Retail Property Activity Rating also increased, from 3.37 to 3.59 over the same 2 quarters. The Office Property Market Activity Rating remained the weakest of the 3, but also rose slightly from 2.97 to 3.32.
- The Near Term Expectations Indices of Property Market Activity, reflecting broker near term expectations, saw the respondents being least optimistic about Office Property, which recorded a mild positive of +12, while the Industrial Property Market recorded a stronger +19. The Retail Sector response surprised, with brokers posting the strongest response in this sector, to the tune of +27.
- In all 3 major property markets, the brokers saw the negative economic impact from COVID-19 lockdowns as still being a major influence on their near term market activity expectations. However, in the Office Sector, the lockdown-related “Zoom Boom” and its potentially major “work from home” implications continued to overshadow even the recession impact, playing a major role in brokers continuing to be least optimistic about the Office Market. The impact of online retail in the Retail Property Sector is seen as far less significant than the “work from home” impact on the Office Market.

## The Methodology

The FNB Commercial Property Broker Survey surveys a sample of commercial property brokers in and around the 6 major metros of South Africa, namely, City of Joburg and Ekurhuleni (Greater Johannesburg), Tshwane, Ethekewini, City of Cape Town and Nelson Mandela Bay.

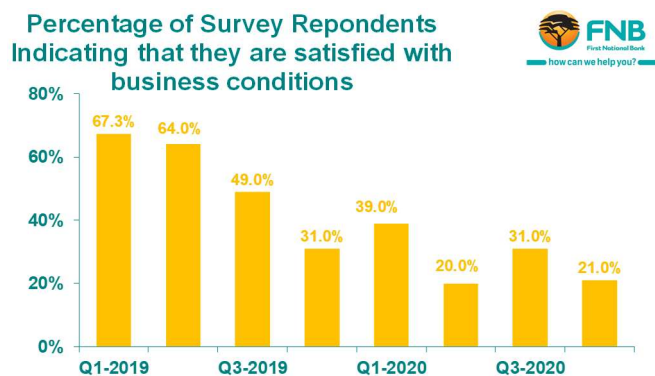
Given FNB Commercial Property Finance's strong focus on the "Owner-Serviced" market, a prerequisite in selecting broker respondents is that they at least deal in owner-serviced properties, but a portion will also have dealings in the developer or investor markets as well as in the listed sector.

In this report we focus on the part of the survey where we ask respondents to rate their perception of the buying/selling market's (i.e. not rental market) activity levels on a scale of 1 to 10, 10 being the strongest activity level rating.

The term "activity" is as experienced by a property broker, and can include everything from indications of interest in buying or selling, e.g inquiries or viewings related to potential buying or listing, through to actual transaction levels.

### After a small increase in the 3<sup>rd</sup> quarter, Broker satisfaction, business conditions deteriorated again in the 4<sup>th</sup> quarter of 2020

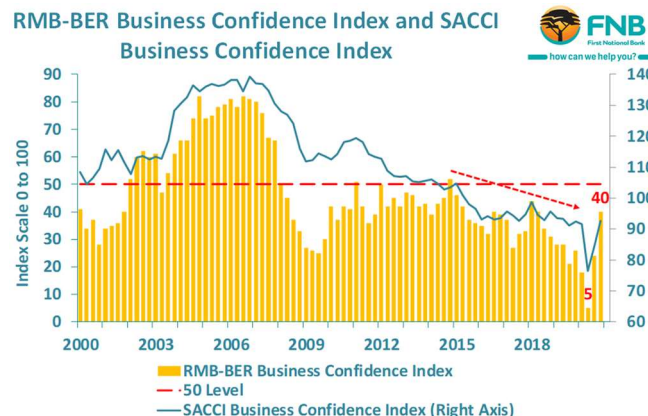
Before we survey activity level perceptions, we ask all respondents to say whether they find business conditions "satisfactory" or not in the form of a simple "yes or no" answer. In the 4<sup>th</sup> quarter of 2020, the percentage of respondents experiencing conditions as satisfactory declined from 31% in the prior quarter to 21%, implying that a major 79% of respondents were still dissatisfied with business conditions as at the time of the November 2020 survey.



This survey response gives a perspective of business confidence in the Commercial Property Sector, which reverted to weakening in the final quarter of 2020 after a once-off 3<sup>rd</sup> quarter increase, now appearing significantly weaker than broader economy-wide business confidence.

Economy-wide business confidence, as portrayed by

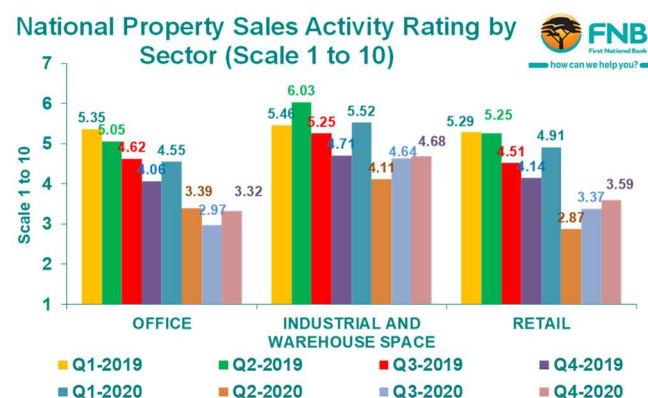
the RMB-BER Business Confidence Index, saw a further increase in the final quarter of 2020, from lockdown low of 5 (scale 0 to 100) in the 2<sup>nd</sup> quarter of 2020 to 24 in the 3<sup>rd</sup> quarter and 40 in the final quarter. However, this reading itself remains weak and reflective of poor confidence levels in a still-deeply recessionary economy.



### Activity Rating by Major Property Class – Office Property perceived as the weakest

When asking brokers for their ratings of market activity levels on a scale of 1 to 10, we still see that the group of respondents is most upbeat (or least pessimistic perhaps) about the Industrial and Warehouse Property Market. This market's 4<sup>th</sup> quarter activity rating rose slightly further, from 4.64 in the previous quarter to 4.68.

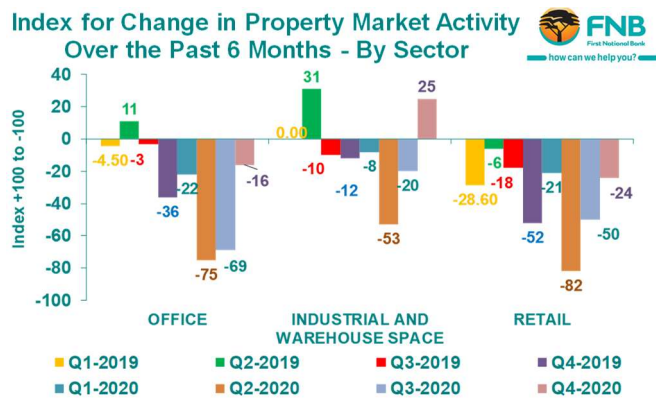
By comparison, the Retail Property Activity Rating was noticeably lower at 3.59 in the 4<sup>th</sup> quarter, although slightly up from its prior quarter's 3.37 reading. The Office Property Market Activity Rating also rose mildly, from a 2.97 low in the 3<sup>rd</sup> quarter to 3.32 in the 4<sup>th</sup> quarter, but remains the weakest rated sector from a buyer-seller market activity point of view.



### Industrial Market Activity was the only sector seen as having strengthened over the prior 6 months

We ask a follow up question as to whether the respondents have perceived a decline, increase or no change in activity levels compared with 6 months prior. From these results we compile an index, allocating a score of +1 to each percentage points'

worth of “increased” responses, zero to that of “unchanged” responses and -1 for that of “decreased” responses. The index is thus on a scale of +100 to -100.



In the 4<sup>th</sup> quarter survey, the market with the highest index reading was the Industrial and Warehouse Property Market. This sector’s reading had improved from the prior quarter’s negative -20, to become the only one with a positive reading of +25 in the 4<sup>th</sup> quarter survey.

This implies that the percentage of respondents perceiving a strengthening in activity in this sector over the prior 6 months exceeds those that perceived weakening by +25 percentage points.

The Office Property Market reading was a far weaker negative of -16, implying that the percentage of respondents perceiving a decrease in activity in this sector exceeded those perceiving an increase by 16 percentage points. This was, however, “less weak” than the previous quarter’s -69.

The Retail Market returned a reading slightly weaker than that of Office, less weak than the previous

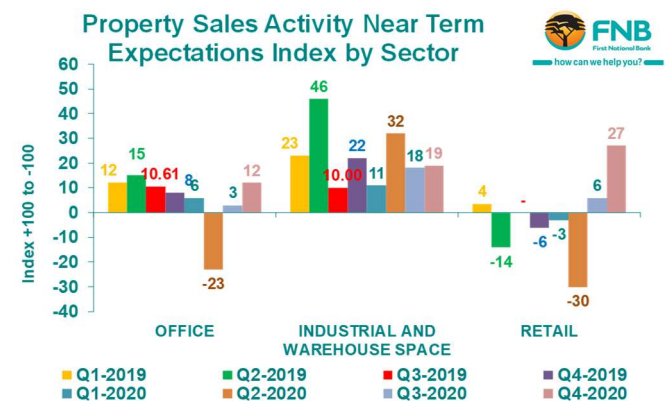
quarter’s -50 but still very soft at -24.

In terms of buyer-seller market activity, the group of survey respondents therefore sees the Industrial Property Market as the strongest of the 3 major segments, although at an activity rating of 4.68 on a scale of 1 to 10, this market can also be seen as “mediocre” at best.

## Outlook – Respondents surprisingly more optimistic about the Retail Market over next 6 months

We compile an index using the same methodology, but this time asking brokers for their expectations of the direction of market activity in the 6 months ahead (“increase”, “stay the same” or “decrease”).

The respondents as a group are now by a small margin the least optimistic about the Office Property Market, which recorded a mild positive +12. The Retail Market reading perhaps surprised on the upside, returning a +27 in the 4<sup>th</sup> quarter survey, and exceeding the +19 recorded by the recently outperforming Industrial Property Sector.



## Key drivers of Brokers’ Expectations – COVID-19 economic impact seen as the biggest influence over the 3 sectors.

In an open-ended follow up question to the one regarding expectations of near-term activity direction, we ask brokers to provide reasons as to why they expect the direction that they do.

The near term expectations regarding activity levels were “moderate”, but pointing to improvement in all 3 property classes on an aggregated basis. But the “improvement” response is a moderate one, and “COVID-19” remained by far the most dominant factor cited as an influence on broker thinking and on their expectations.

- **The Office Market –Remote working prospects challenging Office Property still appear to overshadow the emerging online retail trend that the Retail Property Sector is challenged with.**

In the 4<sup>th</sup> quarter survey, the Office Property component showed 77% of respondents citing “Effect of COVID-19” as a key factor driving their activity expectations.

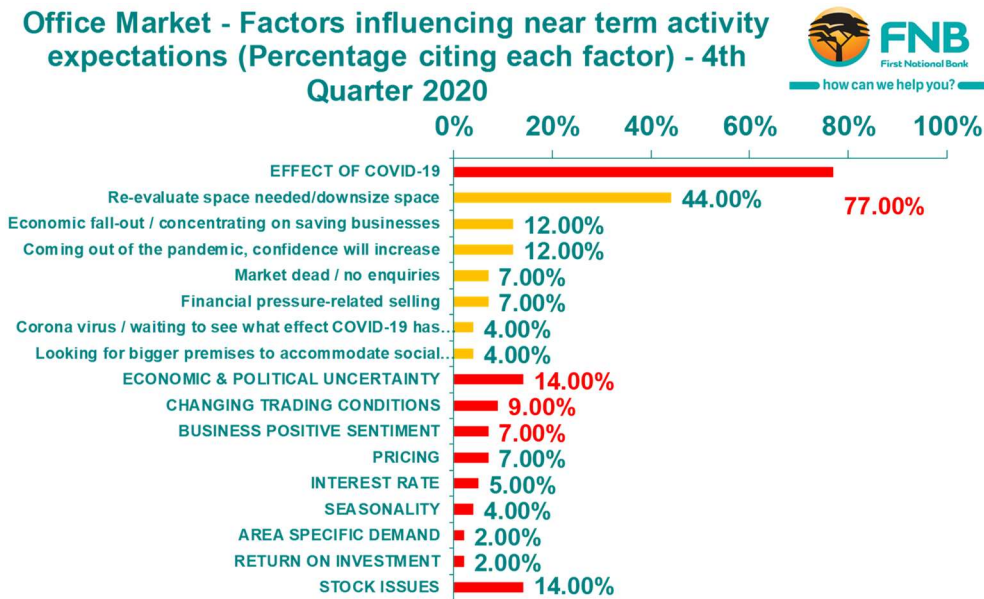
Looking at the sub-components of this key factor is perhaps more insightful though. A very significant 44% of brokers perceive companies to be re-evaluating their office space needs, and in many instances downscaling on office space, thus a key factor influencing their near term expectations of market activity in this segment.

The re-evaluation of office space requirements far exceeds the weak economy and the economic impact of COVID-19 as the most prominent factor in the Office Property Market, as viewed by our survey respondents.

Nevertheless, the weak economy remains a factor in influencing the brokers’ expectations, with 12% pointing to the

economic fallout emanating from the COVID and its lockdown period, and another 14% citing “Economic and Political Uncertainty, a factor that has been around since before the pandemic.

A further noticeable factor cited was that of “Stock Issues”, which was mentioned by 14%. Only 2% of brokers pointed to stock constraints, while a greater 12% pointed to an oversupply of stock.



• **The Industrial and Warehouse Market**

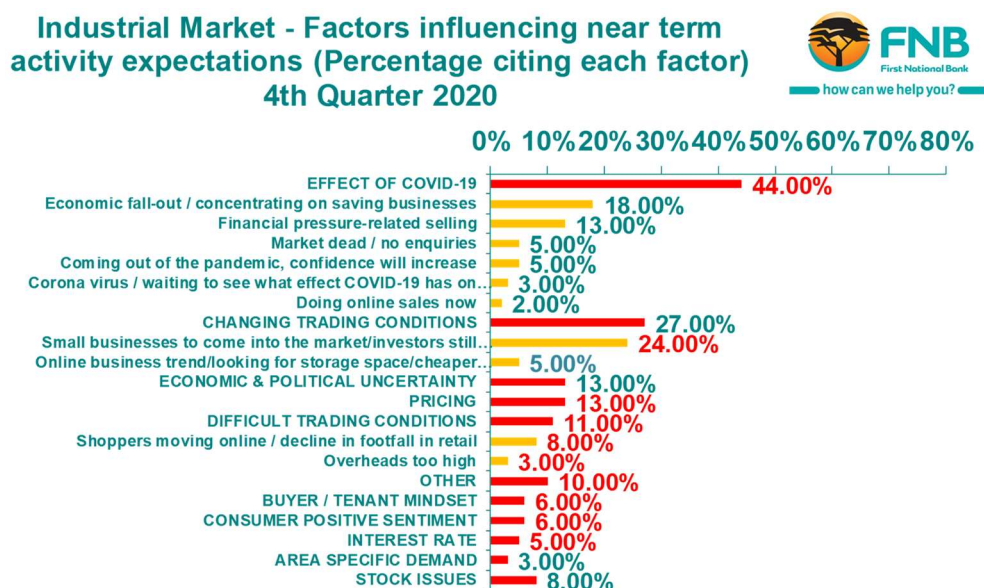
In the Industrial and Warehouse Property Market survey component, the “Effect of COVID-19” was also the major factor, with 44% of survey respondents pointing to the economic fallout from COVID-19 lockdowns as being a key issue in influencing their near term market activity expectations. Within this general category of response, 18% cited the economic fallout from COVID-19, while 13% cited “Financial Pressure-related selling”, also very strongly economy-linked.

However, some noticeable positives come through in this survey response too. Industrial Property is the most affordable property category of the 3 major property classes, and 24% believe it to be appealing amongst smaller businesses, while investors “still find value” in this property class.

The “Economic and Political Uncertainty” category remains noteworthy, with 13% of brokers pointing to this as a factor, and coupled with those citing the direct and indirect economic impacts of COVID-19, it makes economic weakness a major constraining factor.

8% of respondents see positives from online retail, perceiving more warehouse space to be required as a result.

The broker surveys thus do bring out industrial property’s relative affordability as being something of a competitive advantage over the other 2 major classes.



- **The Retail Property Market**

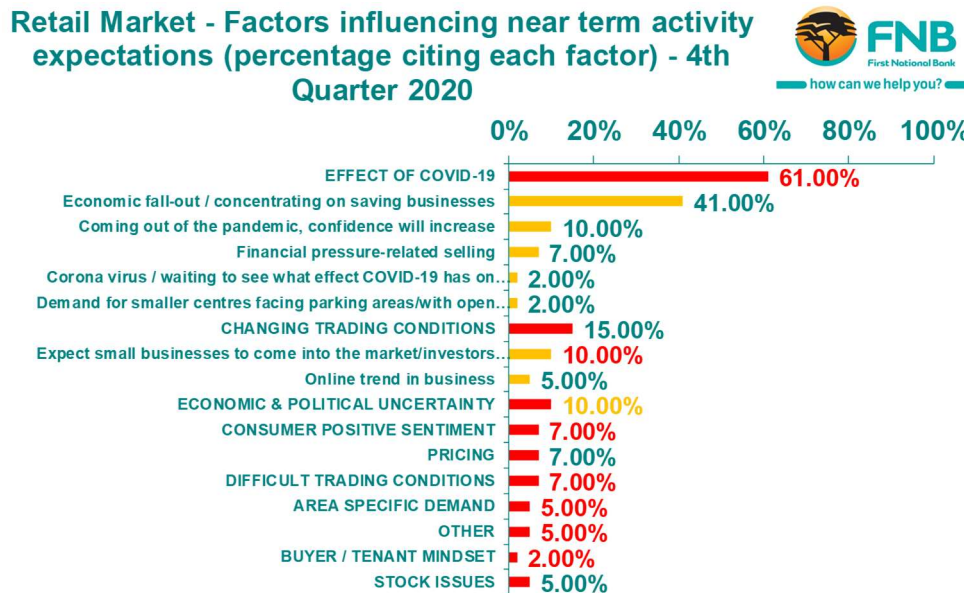
The brokers appear to see the emergence of online retail as only a minor current issue.

Rather, the broker respondents still see the COVID-19 impact, and the recessionary impact of the lockdowns, as by far the main issue that the Retail Property Sector faces.

61% of respondents see the Impact of COVID-19 as key, and within that major response category 41% of brokers see the economic fallout of COVID-19 as a key factor influencing their expectations.

By comparison, only 5% of respondents cite online retail affecting footfall in centres.

Therefore, the broker group still sees general economic performance and its impact on consumer purchasing power as the key issue for retailers and their landlords.



## Conclusion

The 4<sup>th</sup> quarter 2020 FNB Property Broker Survey was undertaken during November, at which stage South Africa had long-since passed on from the “hard” COVID-19 lockdowns of the 2<sup>nd</sup> quarter, but had not yet seen a major uptick in new daily Covid-19 cases in what has more recently become the 2<sup>nd</sup> major infections surge.

While economic activity had rebounded significantly during the 3<sup>rd</sup> quarter, following the end of the 2<sup>nd</sup> quarter “hard lockdown”, GDP levels had probably not yet returned to pre-COVID-19 levels, according to 4<sup>th</sup> quarter high frequency economic data already released.

In other words, in the late stages of 2020 when this survey was undertaken, the economy that was already weak prior to 2020, was likely even weaker than 2019. Therefore, it is not surprising to see the broker business confidence survey component continue to show the overwhelming majority of respondents being dis-satisfied with business conditions.

Given South Africa’s myriad of well-documented structural economic problems (An unreliable and increasingly expensive electricity supply and steadily deteriorating Government finance and debt situation,

to name but 2), the negative economic impacts from the 2<sup>nd</sup> quarter hard lockdowns could be expected to linger. And indeed in this survey it is the negative economic impact from COVID-19 lockdowns on the property market that still comes out most strongly as a key issue in influencing broker near term market activity expectations.

Nevertheless, Brokers perceived mild market activity improvements in the 4<sup>th</sup> quarter survey, compared to the previous quarter, albeit still weak levels of activity.

In addition, they expected some moderate near term improvement in activity levels early in 2021 in all 3 property sectors.

However, it must be borne in mind that the survey was done prior to the 2<sup>nd</sup> virus infections surge getting under way, and prior to any thought perhaps of renewed stricter lockdown regulations and heightened consumer “fear”.

The February 1<sup>st</sup> quarter 2021 broker survey will give us greater insight into whether the 2<sup>nd</sup> virus surge dampened matters once more.

Finally, Globally there has been ongoing debate around the “work-from-home” trend and whether it will or won’t impact heavily on office space demand. There are those that see imminent downscaling of

office space requirements by many companies, and a resultant major glut of office space. Recently, however, some “naysayers” have been fighting back, citing the need for office space to enhance human collaborations, the argument being that working online full time has limitations in terms of human relationships.

Such arguments have validity. But the broker survey still points to a very strong broker perception that many companies are indeed revising their office needs lower, and the brokers do perceive activity in the office market to be the weakest of the 3 major sectors.

We would have expected such a perception. While office space has its place for physical meeting and

interaction, our belief is that less of it is needed for such purposes, with staff able to spend a very significant part of their time at home. In addition, financial realities for pressured companies may play a key role in decision-making, and office space is costly.

But finally, regardless of the “pros and cons” arguments around remote work”, recent SAPOA office vacancy data points to an acceleration in the rising national office vacancy trend. Whether that is purely financial pressure-related downscaling or “work-from-home”-specific thinking, the end result looks set to be the same, i.e. very weak demand for office space, and increased over-supply.

## Disclaimer

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